

### **U.S. Financial Services Industry**

Contributing to a More Competitive US Economy

JULY 2010

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The financial services industry is a vital component of the US and world economies. It provides the fuel that promotes job creation and sustains economic growth and innovation. A robust finance industry provides businesses with new ways to lower the cost of capital, stimulates global investment and trade, and presents investors with a broad array of products and services to increase return and manage risk. Importantly, these financial services and products help facilitate and finance the export of manufactured goods and agricultural products, while helping the US become the world's number one exporter of services. The long-term health and vigor of this sector, and its ability to service customer needs, depends on its ability to remain competitive both at home and abroad.

A vibrant US financial services sector requires having access to clients not only in the US, but in markets around the world. And why are these non-US markets essential for future US economic growth and job creation? The answer lies in the growing market share of non-US markets — more than three-quarters of the world's GDP, about two-thirds of the world's equity market capitalization, approximately two-thirds of the world's debt markets, and 95 percent of the world's consumers, are now found outside the United States. As the table below shows, these trends are especially strong in the rapidly growing "BRIC" countries (Brazil, Russian, India, and China). Underscoring growth in the BRICS — current estimates indicate that the BRICs will account for 50% of global GDP by 2050.¹ Not surprisingly, many of the best future growth opportunities for the global companies lie in non-US markets.

Goldman Sachs Global Economics, Commodities and Strategy Research, November 4, 2009.

## Timeline for BRICs to Overtake G6 Gross Domestic Product

	France	Germany	Italy	Japan	UK	US
Brazil	2027	2029	2020	2034	2038	
China	2006	2008	2004	2010	2006	2027
India	2021	2024	2017	2027	2023	
Russia	2024	2029	2017	2037	2027	

Source: The Long-Term Outlook for the BRICs and N-11 Post Crisis, Goldman Sachs Global Economics

The primary motivation for financial services firms to operate in non-domestic markets is to follow their multinational clients and become better acquainted with the markets in which they operate so they can provide the financial tools and products to among other things raise capital and manage risk. Multinational companies and investors seek the global expertise of financial services firms for a wide array of activities — research, fund management, corporate finance, and risk management, to name a few. To compete effectively and serve their customers, many of whom operate and raise capital in global markets, financial services firms must have the capabilities to establish a local presence in many markets around the world, while providing other services on a cross-border basis. Access to non-US markets enhances the competitiveness of the US financial services industry, benefitting its more than 5.77 million US employees, and further strengthening the entire US economy.

#### A Vital Component of the U.S. Economy

The US services sector is the most dynamic component of the US economy, accounting for over three-quarters of total US employment. The services sector also accounted for more than 78 percent of US Gross Domestic Product (GDP) in 2009.<sup>2</sup> Without question, this sector dominates the economy and will be the springboard for future US economic growth. During the period 1998-2008, for example, services industries added nearly 14 million jobs, in contrast to the loss of over 2.9 million jobs in goods-producing industries.<sup>3</sup> The shift to a more services-oriented economy is more than a short-term phenomenon; the US Bureau of Labor Statistics (BLS) projects future job growth to mirror this trend. BLS employment projections for 2008-2018 show that of a projected 14.6 million increase in employment, service industries will account for virtually all of the job growth.<sup>4</sup>

<sup>&</sup>lt;sup>2</sup> U.S. Department of Commerce, Bureau of Labor Statistics, 'Employment by Sector', January 2010

<sup>&</sup>lt;sup>3</sup> U.S. Department of Commerce, Bureau of Labor Statistics, 'Employment by Sector', November 2009

<sup>&</sup>lt;sup>4</sup> U.S. Department of Commerce, Bureau of Labor Statistics, 'Employment by Sector', November 2009

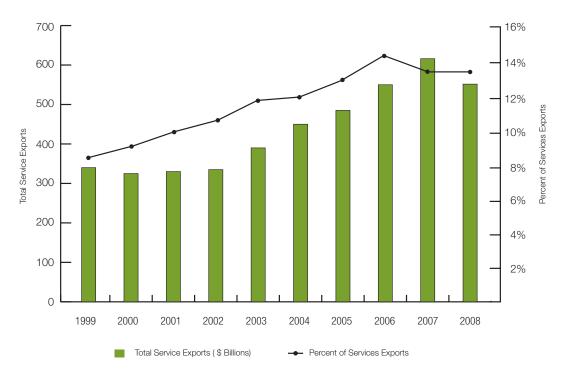
Financial services export: source of US job growth. Within the services sector, the financial services industry employs some 5.77 million individuals, about six percent of total private non-farm employment. Employment in the securities sub-sector (including broker-dealers, commodities, and other financial investments and related activities) is projected to expand 12 percent by 2018, spurred by the large number of baby boomers in their peak savings years, the growth of tax-favored retirement plans, and the globalization of securities markets.<sup>5</sup> Interestingly, rapid expansion of the financial services sector abroad has been accompanied by increased employment in the US.

The wealth generated by the financial services industry contributed nearly 6 percent, or more than \$828 billion, to 2009 US GDP. The most recent data available (2000-2008) indicates contributions by the sector remain an important and growing portion of GDP. As an overall contributor to the US GDP, the services sector grew by more than \$120 billion during 2009, while the financial services industry grew by more than \$16 billion. The substantial contribution of the financial services industry is supported, in part, by the export of financial services and products. In 2008 (latest export data available), US financial services firms exported \$70.9 billion of financial products and services, and garnered a surplus of more than \$8.9 billion.<sup>6</sup> These exports continue to generate significant employment opportunities within the US.

<sup>&</sup>lt;sup>5</sup> U.S. Department of Commerce, Bureau of Labor Statistics, 'Overview of 2008-2018 Projections,'

<sup>&</sup>lt;sup>6</sup> Financial services exports totaled \$60.2 billion (with a surplus of \$41 billion), while insurance exports of financial goods and services exported \$10.8 billion.

# US Exports of Financial Services and Products Are Nearly 13% of All US Services Exports

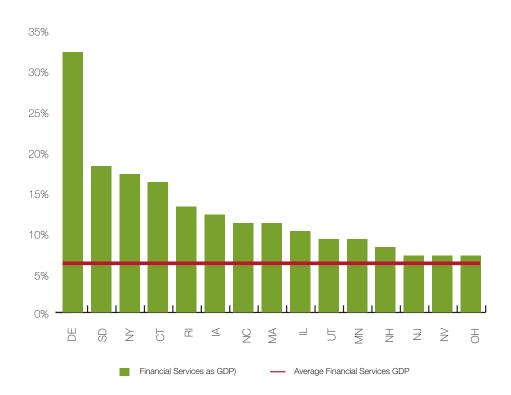


Given the capital-intensive nature of the operations and data processing functions in financial services firms, U.S. jobs related to such critical support functions will continue to expand. As foreign affiliates generate new business, support services in the US will expand to meet the additional volume. Because technology has made it possible to conduct such support functions off site, the foreign affiliates can take advantage of economies of scale and "piggyback" off the US parent's existing systems, thus reducing the firm's overall costs. Other areas that use the expertise of specialists — such as portfolio management, research, and new product development — will similarly benefit as firms draw on the capital-intensive infrastructure already in place in the US for their operations in foreign markets. These US facilities serve as "factories" which develop the financial service products US companies sell abroad.

Role in economies of US states. The financial services industry plays an equally important role in state and local economies and is a vital component of many states' revenue streams. In nearly half the country, the industry provides for 6% or more of state gross domestic product. In traditional financial hubs such as New York and Massachusetts, the industry accounted for 16.4% and 9.7% of overall state GDP, respectively, in 2008. The sector also supports a significant number of jobs and tax revenue in states such as Illinois, Pennsylvania, Texas, Florida, Connecticut, Georgia, South Dakota and Delaware, where the industry directly employs at least 20,000 individuals in each state.7

<sup>&</sup>lt;sup>7</sup> Bureau of Economic Analysis, of Commerce. "Significant" is defined as more than 5% of overall GDP per state.





States greater than average contributions to GDP from the financial services and insurance sector. Source BLS data

#### Links to the Global Economy

To be fully competitive, US companies must span the globe, from large developed markets such as the European Union, to smaller developing markets like Vietnam. US goods and services firms want to expand to foreign markets because the US economy only accounts for about 27% of total world output.8 Confronting mature markets in the US, multinational companies increasingly rely on foreign markets to boost sales and develop new sources of income. And, as multinational companies seek to expand their global footprint by selling cars in fast growing emerging markets, or providing infrastructure investments for roads, electricity, and technology development, these companies must have the financial tools that only global financial services firms can provide.

In order for the financial services industry to help multinational companies take advantage of these global opportunities, they must have ability to provide, for example, currency related products, deal with cross-border tax differences, offer country risk assessments, develop global cash management facilities, and provide country-specific investment advice and solutions: all key services provided by global financial institutions to promote US exports.

<sup>8</sup> IMF Global Financial Stability, 2008 Appendix Table 3,

Financial firms adjust scale to meet needs of global market. To provide these services to their clients, global financial institutions have developed platforms in order to offer their services on a cross-border basis, or thorough the establishment of local offices. In this way, financial services firms have set up the infrastructure to help multinationals navigate through the complexities of trade and investment flows that span geographic regions and economies. That is why large global financial institutions can have a third or more of their asset-base outside their "home" country as many financial services require direct knowledge of local regulation, market practices and other requirements. The global reach of these firms creates economies of scale and scope where firms combine different products and services, resulting in greater savings for the customer. Global firms are able to afford the overhead costs of building global platforms and systems for carrying out global trade and finance in a manner that smaller purely domestic firms cannot. As the size of a bank's customers grows, they require a broader and more sophisticated product suite and demand that these products be offered on a large scale, global basis. The credit demands of a large multinational corporation are larger, broader, and more global. Big banks with ample balance sheets and global reach are required to service these customers.

Financial firms enrich domestic capital markets and build export markets. Global financial services firms also play an important developmental role by encouraging increased dissemination of information, enhancing price discovery, and lowering transaction costs. The products and services they provide in the local markets facilitates access to capital by making it cheaper and more plentiful, provides a broader and more tailored variety of products to investors, mobilizes and increases capital investment in local businesses, enhances productivity, and promotes balanced growth. This, in turn, supports economic growth and job creation. Consequently, global investors will benefit from more attractive investment opportunities, exporters will be able to access to a more vibrant export market for goods and services, and workers will benefit from increased job opportunities.

#### Conclusion

As the US share of global output and its financial markets becomes relatively smaller, access to foreign markets is of increasing importance to global financial services firms. As multinational clients continue to expand their global capabilities and establishment in foreign markets, US firms need to follow these clients to remain competitive. Financial institutions provide the services which facilitate the entry of companies into international markets. As fiscal belt-tightening limits the government resources available, US companies will increasingly rely on US financial services firms to raise the funds necessary to enter and be competitive in foreign markets. Clearly, the financial services sector must have access to world capital markets to raise the lowest cost capital and provide the advice necessary to help a company establish a profitable presence in a foreign market. As the US seeks to increase the standard of living for its citizens, economic growth, job creation and the ability to compete internationally will be critical ingredients in achieving this goal.

July 28, 2010